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No. 250

In the Supreme Court of the United States

OCTOBER TERM, 1951

THE UNITED STATES OF AMERICA, APPELLANT,

vs.

NEW WRINKLE, INC., AND THE KAY & FAS COMPANY.

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF OHIO

STATEMENT AS TO JURISDICTION

IN THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF OHIO WESTERN DIVISION

Filed July 24, 1951

Civil Action No. 1006

UNITED STATES OF AMERICA, PLAINTIFF,

vs.

NEW WRINKLE, INC., AND THE KAY & ESS COMPANY, DEFENDANTS.

STATEMENT AS TO JURISDICTION

In compliance with Rule 12 of the Supreme Court of the United States, as amended, the United States of America submits herewith its statement particularly disclosing the basis upon which the Supreme Court has jurisdiction on appeal to review the judgments of the district court entered in this cause on June 5, 1951. A petition for appeal is presented to the district court herewith, to wit, on July 24, 1951.

OPINION BELOW

No opinion was filed by the District Court for the Southern District of Ohio.

JURISDICTION

The jurisdiction of the Supreme Court to review by direct appeal the judgments entered in this cause is conferred by Section 2 of the Expediting Act of February 11, 1903, 32 Stat. 823, 15 U.S.C. 29, as amended by Section 17 of the Act of June 25, 1948, 62 Stat. 869.

The following decisions sustain the jurisdiction of the Supreme Court to review the judgments on direct appeal in this case:

United States v. *United States Gypsum Co.*, 333 U.S. 364.

United States v. *National Assn. of Real Estate Boards*, 339 U.S. 495.

QUESTIONS PRESENTED

1. Whether an agreement by patentees for a patent licensing program to fix prices for an entire industry, with conscious participation in such program by the licensees thereunder, violates Section 1 of the Sherman Act.

2. Whether price fixing achieved through assignment of patents by two patentees to a corporation organized by them to license and fix prices is sanctioned by the patent law, and hence not within prohibitions of the Sherman Act.

3. Whether the ruling in *United States* v. *General Electric Co.*, 272 U.S. 476, authorizes a non-manufacturing patentee to fix the minimum prices at which its licensees may sell products manufactured under its patents.

STATUTE INVOLVED

The pertinent provisions of Sections 1 and 4 of the Act of July 2, 1890, 26 Stat. 209, as amended

(15 U.S.C. 1, 4), commonly known as the Sherman Act, are as follows:

> Sec. 1. Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is hereby declared to be illegal: * * *. Every person who shall make any contract or engage in any combination or conspiracy hereby declared to be illegal shall be deemed guilty of a misdemeanor, * * *.
>
> Sec. 4. The several district courts of the United States are hereby invested with jurisdiction to prevent and restrain violations of this act; and it shall be the duty of the several district attorneys of the United States, in their respective districts, under the direction of the Attorney General, to institute proceedings in equity to prevent and restrain such violations. * * *

STATEMENT

This is a civil action filed in September 1948 alleging a conspiracy to restrain interstate and foreign commerce in wrinkle finishes in violation of Section 1 of the Sherman Act. The complaint names two defendants—New Wrinkle, Inc., a non-manufacturing patent licensor, and The Kay & Ess Company (referred to herein as K&S), a manufacturing licensee—and a number of co-conspirators comprising the various manufacturers of wrinkle finishes licensed under the patent rights of New Wrinkle, together with Chadeloid Chemical Company (referred to herein as Chadeloid), a corporation which was dissolved in 1945. Separate motions to dismiss the complaint were filed by the defendants. The motions were argued

in February 1949, and on June 5, 1951, more than 27 months later, the district court entered orders of dismissal. No opinion was filed, but the court's orders recite that the motions to dismiss are "well taken."

The principal allegations of the complaint (admitted by the motions to dismiss) are as follows:[1]

For many years, the defendants and their co-conspirators have been engaged in a conspiracy to restrain interstate and foreign commerce in wrinkle finishes (par. 13). These finishes are enamels, varnishes and paints which produce a hard wrinkled surface when applied to metal or other material (par. 8). They have important advantages over ordinary enamels and varnishes and are widely used as surface coverings for typewriters, cash registers and many other articles (par. 9). The licensees of New Wrinkle manufacture "substantially all" of the wrinkle finishes produced in the United States, "a substantial portion" of which finishes are sold and shipped in interstate and foreign commerce (par. 12). Manufacturers of wrinkle finishes receive more than $2,000,000 annually from the sale of their products (par. 10).

Prior to and during 1937 K&S and Chadeloid were engaged in litigation over their respective patents relating to wrinkle finishes (par. 14). Chadeloid claimed that its patents were basic and that the K&S patents, which covered allegedly more efficient methods of manufacture, were subservient to its patents (*ibid.*). During 1937

[1] A copy of the complaint (not including the Exhibits attached thereto) is attached hereto as Appendix A.

the two companies negotiated with a view to effecting a pooling of their patents in order to eliminate competition between themselves and to set up a licensing system under which "prices for the entire wrinkle finish industry would be fixed" (par. 13). The negotiations resulted in a contract which they entered into on November 2, 1937 (par. 16). This contract provided: A new corporation (defendant New Wrinkle) was to be organized. K&S and Chadeloid agreed to assign their wrinkle finish patents to the new corporation in exchange for its stock. New Wrinkle was to grant patent licenses to the various manufacturers of wrinkle finishes (including K&S and Chadeloid), and was to fix "minimum prices at which all licensed manufacturers might sell" (*ibid.*). The price schedules were not to be effective until the Sherwin-Williams Company and eleven other companies (of those named as principal manufacturers of wrinkle finishes in a list attached to the contract) had signed license agreements and agreed to follow the prescribed minimum prices (*ibid.*).

Following incorporation of New Wrinkle and transfer to it of the patent rights of K&S and Chadeloid, these companies and certain of the companies named as co-conspirators worked together to induce other manufacturers to accept patent licenses from New Wrinkle in order that competitive practices which they deemed undesirable might be eliminated (par. 18). Prospective licensees were advised that other prospective licensees were being consulted "in order to establish minimum prices throughout the industry"

(*ibid.*). Meetings were held at which the terms of the licenses to be granted by New Wrinkle were agreed upon, and prices, terms, and conditions of sale were discussed (par. 19). Various manufacturers signed license agreements but price schedules were not put into effect until the Sherwin-Williams Company and eleven of the other companies listed in the agreement of November 2, 1937, had agreed to accept licenses (*ibid.*). After May 7, 1938, when the price schedules were made effective, various other manufacturers signed license agreements, and did so with knowledge that concerted action was contemplated and required in order to carry out the conspiracy to which the defendants were parties (par. 21). When the complaint was filed, more than 200 manufacturers of wrinkle finishes held patent licenses granted by New Wrinkle (par. 11).

All of New Wrinkle's patent license agreements are substantially identical (par. 21). They authorize the licensor to establish a "Schedule of Minimum Prices, Discounts, and Selling Terms," and further provide that the prescribed prices and terms shall not be binding upon the licensee unless the same terms are imposed upon all other licensees (Exhibit C,[2] par. 7).

From time to time New Wrinkle has established schedules of minimum prices and terms of sale (par. 22). The schedule in effect at the time the complaint was filed provides, among other things: A licensee violates the price schedule if he sells other products at "special cut prices" for the

[2] Exhibits C and D are attached to and made a part of the complaint (pars. 21, 22).

purpose of influencing sale of wrinkle finishes (Exhibit D, p. 2). He may sell "clear" wrinkle finish (the lowest priced product) only for use as such, and if the purchaser converts it to a colored finish, he must be charged the price fixed for colored wrinkle finish (*id.*, pp. 2, 5). The licensee may give discounts only as authorized by New Wrinkle's price schedule and only after receipt of a written supporting statement, a copy of which is to be attached to the licensee's next report to the licensor (*id.*, p. 4). The cash discount which the licensee may grant is also specified and rigidly limited (*id.*, pp. 4, 5).

Defendants intended that their conspiracy should fix identical and unreasonably high minimum prices for "substantially all wrinkle finishes manufactured and sold in the United States," and should eliminate competition between defendants and the co-conspirators in the sale of such finishes (par. 23). The conspiracy has had such effect (*ibid.*).

THE QUESTIONS ARE SUBSTANTIAL

1. The district court evidently accepted the defendants' contention that the holding in *United States* v. *General Electric Co.*, 272 U.S. 476,—that the patent law authorizes a patentee to license his patent with provisions fixing the licensee's minimum sales price—sanctions the price-fixing method here involved.[3] It is the Government's

[3] New Wrinkle also contended that mere licensing is not commerce and that New Wrinkle's licensing activities are therefore not in restraint of interstate commerce. This contention appears almost frivolous. The complaint charges fixing of the sales price of licensees and alleges that "a substantial portion" of the licensees' products are sold and shipped in interstate commerce.

contention that the allegations of the complaint bring the case squarely within the rulings of the Court in *United States* v. *United States Gypsum Co.*, 333 U.S. 364, 339 U.S. 959, 340 U.S. 76, and that the district court should therefore have denied defendants' motions to dismiss and permitted the case to go to trial.

In the *Gypsum* case the Court in its opinion on the Government's second appeal stated the grounds (340 U.S. 83-88) for its *per curiam* dismissal of the defendants' appeal from the summary judgment entered against them. The Court declared that concert of action between a patentee and those who become its licensees, to fix prices throughout an industry through the medium of patent licenses, violates the Sherman Act, and is not within the implied exception from its prohibitions of monopoly rights conferred by patent law. The Court further stated that the terms of the license agreements and other admitted facts established conscious concert in price fixing and that, since such conduct is in itself a violation of the Sherman Act, it would not be taken out of the reach of the Act by proof that there had been no agreement among the defendants to "associate themselves in a plan to blanket the industry under patent licenses and stabilize prices."

The complaint in the instant case expressly alleges agreement by the defendants upon a patent licensing program to fix prices for the entire wrinkle finish industry, and conscious participation in that program by those licensed pursuant thereto. Such allegations set forth an arrangement of the precise kind condemned in the *Gypsum* case. We

therefore submit that the district court's action in dismissing the complaint contravenes established limitations of the holding in the *General Electric* case. Upon the facts admitted by the motions to dismiss, the defendants are engaged in illegal price fixing, and the judgments of dismissal leave them free to continue this unlawful conduct.

2. This appeal also raises the question whether the combination of patents described in the complaint is illegal under the doctrine of *United States* v. *Line Material Co.*, 333 U.S. 287. The Court there held that the patent law does not sanction cross-licensing by two patent owners under an arrangement giving to one owner authority to grant price-fixing licenses under the patents of both. Clearly the Sherman Act would have been violated if K & S and Chadeloid had cross-licensed each other, with power in one to grant price-fixing licenses under the patents of both companies. The same fixing of prices was achieved through combining separately owned patents when K & S and Chadeloid organized New Wrinkle and assigned their patents to it for the purpose of granting price-fixing licenses thereunder. The Government submits that the holding in the *Line Material* case equally applies in this situation. This Court unanimously condemned as early as 1912 price limitation effected through assignment of patents to a third person to act as licensor. *Standard Sanitary Mfg. Co.* v. *United States*, 226 U.S. 20.

3. The rationale of permitting a patentee to fix the prices at which his licensee sells was stated in the *General Electric* case as follows: "When the patentee licenses another to make and vend and

retains the right to continue to make and vend on its account, the price at which his licensee will sell will necessarily affect the price at which he can sell his own patented goods." 272 U.S. at p. 490. Since New Wrinkle, the patentee here, does not manufacture or sell the patented products, protection against price-cutting by its licensees cannot be considered as "normally and reasonably adopted to secure pecuniary reward for the patentee's monopoly" (*ibid.*).[4] The appeal therefore presents the substantial question of whether the General Electric case authorizes a *non-manufacturing* patentee to fix the prices at which its licensees sell.

We believe that the questions presented by this appeal are substantial and that they are of public importance.

Respectfully submitted,

(S.) PHILIP B. PERLMAN,
Solicitor General.

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[4] Even with respect to royalty, the licensees' sales prices are immaterial. The royalty payable to New Wrinkle is the flat sum of 5¢ per gallon (Complaint, par. 20).

APPENDIX

IN THE DISTRICT COURT OF THE UNITED STATES FOR THE SOUTHERN DISTRICT OF OHIO

Civil Action No. 2276

Filed September 21, 1948

UNITED STATES OF AMERICA, PLAINTIFF,

v.

NEW WRINKLE, INC., AND THE KAY & ESS COMPANY, DEFENDANTS.

COMPLAINT

The United States of America, by its attorneys, acting under the direction of the Attorney General, brings this action against the defendants and complains and alleges as follows:

I

JURISDICTION AND VENUE

1. This complaint is filed and this action is instituted against the defendants under Section 4 of the Act of Congress of July 2, 1890, c. 647, 26 Stat. 209, as amended, entitled "An Act to protect trade and commerce against unlawful restraints and monopolies," commonly known as the "Sherman Act," in order to prevent and restrain continuing violations by the defendants, as hereinafter alleged, of Section 1 of said Act.

2. Each of the defendants transacts business within the Southern District of Ohio and is found therein.

II

THE DEFENDANTS AND CO-CONSPIRATORS

Defendants

3. New Wrinkle, Inc., hereinafter referred to as New Wrinkle, a corporation organized and existing under the laws of the State of Delaware, with its principal offices at Dayton, Ohio, is made a defendant herein.

4. The Kay & Ess Company, hereinafter referred to as K & S, a corporation organized and existing under the laws of Ohio, with its principal offices at Dayton, Ohio, is made a defendant herein.

Co-conspirators

5. Chadeloid Chemical Company, hereinafter referred to as Chadeloid, a corporation organized under the laws of West Virginia, is not made a defendant, but is named a co-conspirator herein. Chadeloid was dissolved in or about the year 1945 and its assets distributed among its stockholders.

6. The manufacturing concerns listed on Exhibit A attached to this complaint are not made defendants, but are named co-conspirators herein. Each is, or has been during the period covered by this complaint, a licensee under the wrinkle finish patent rights owned or controlled by New Wrinkle, Inc., and each is, or has been during that period, engaged in manufacturing and selling wrinkle finishes, as defined below.

7. Certain individuals from time to time associated with or acting on behalf of one or more of the defendants or co-conspirators have also acted as co-conspirators in the offenses charged herein.

III

Nature of the Trade and Commerce Involved

8. "Wrinkle" finishes, also known as "Crinkle," "Shrivel," "Sag," "Morocco," and by other designations, are defined as enamels, varnishes and paints which have been compounded from such materials and by such methods as to produce, when applied and dried, a hard wrinkled surface on metal or other material.

9. Wrinkle finishes are widely used as coverings for the surfaces of typewriters, cash registers, motors, adding machines, and many other articles of manufacture. They have the following advantages over smooth finishes such as ordinary enamels and varnishes:

a. One coat of wrinkle finish is sufficient for many purposes for which two or more coats of smooth finish would be required;

b. Surfaces to which wrinkle finishes are to be applied need not be prepared as carefully as those which are to receive smooth finishes, since the wrinkle finishes cover small imperfections; and

c. The original appearance of wrinkle-finished articles can be maintained with less cleaning and polishing than that of smooth-finished articles.

10. Wrinkle finishes are being produced and sold in the United States at the rate of approximately one million gallons per year and the manufacturers thereof receive in excess of two million dollars per year for these products.

11. New Wrinkle has not engaged in the commercial manufacture and sale of wrinkle finishes at any time since its incorporation in 1937. However, it owns or controls patents relating to wrinkle finishes, and since 1938, has licensed and now

licenses in excess of 200 manufacturing concerns to make, use, and sell wrinkle finishes under those patents.

12. Substantially all wrinkle finishes produced in the United States are manufactured by these licensees, whose places of business are located in principal cities throughout the various states. A substantial portion of the wrinkle finishes made by licensees is sold to purchasers in states other than those in which the finishes are manufactured and to purchasers in the Dominion of Canada, and is shipped from one state to another, and from various states of the United States to various locations in the Dominion of Canada in the ordinary course of business.

IV

Offenses Charged

13. For many years, the defendants and co-conspirators have been continuously and are now engaged in an unlawful combination and conspiracy, and have been continuously and are now parties to unlawful contracts, in restraint of trade and commerce in wrinkle finishes among the several states of the United States and between various states of the United States and the Dominion of Canada, all in violation of Section 1 of the Sherman Act. The defendants and co-conspirators are continuing, and threaten to and will continue said offenses unless the relief hereinafter prayed for in this complaint is granted. The aforesaid combination and conspiracy, and certain of the contracts, agreements, arrangements and understandings which formed a part and were used in effectuation thereof will be hereinafter more fully set forth and described.

14. In 1937, and for some time prior thereto, K & S and Chadeloid had been engaged in litigation with respect to various patents on wrinkle

finishes. Chadeloid held certain patents which it alleged were basic; K & S held other patents which it alleged provided for more economical and efficient means of producing wrinkle finishes, but which Chadeloid contended were subservient to the basic patents held by Chadeloid.

15. During 1937 representatives of K & S and Chadeloid negotiated with each other with a view toward effecting a pooling of the patents of the two corporations in order to eliminate competition between them and to set up a licensing system under which prices for the entire wrinkle finish industry would be fixed.

16. As a result of these negotiations, on or about November 2, 1937, K & S and Chadeloid entered into a contract providing for the formation of a new company to be known as New Wrinkle, Inc., to which K & S and Chadeloid each agreed to assign all of its patent rights relating to wrinkle finishes in return for common and preferred stock in the new corporation. The contract further provided that non-exclusive licenses under all the wrinkle finish patent rights previously held by K & S and Chadeloid would be granted by New Wrinkle to Chadeloid, K & S, and other manufacturers of wrinkle finishes, and that minimum prices at which all licensed manufacturers might sell would be fixed by New Wrinkle. Attached to the contract was a list of the principal companies then engaged in the manufacture and sale of wrinkle finishes and it was expressly agreed that the price schedules would not be made effective until the Sherwin-Williams Company, a corporation of Ohio with its general office at Cleveland, Ohio, and any eleven of the other companies on the list had signed the contract and agreed to follow the minimum prices. A copy of the list is attached to and made a part of this complaint as Exhibit B.

17. After the formation of New Wrinkle, and

the transfer to it of the patent rights previously held by K & S and Chadeloid, provided for in the aforesaid contract of November 2, 1937, the new corporation caused its stock to be issued on the following basis:

To K & S: 150 shares of preferred and 51% of the common stock.

To Chadeloid and its nominee: 400 shares of the preferred, and 49% of the common stock.

18. After the execution of the aforesaid contract, representatives of K & S and of Chadeloid worked together and with representatives of certain of the companies named as co-conspirators to induce the other companies in the industry to accept licenses from New Wrinkle in order that competitive practices deemed by them to be undesirable might be eliminated. Prospective licensees were advised that other prospective licensees had been and were being consulted in order to establish minimum prices throughout the industry.

19. Meetings were held between representatives of K & S and Chadeloid and of certain of the co-conspirators at which terms of the license agreements were agreed upon, and prices, terms, and conditions of sale were discussed. Licenses were then executed between New Wrinkle and certain of the co-conspirators; but as provided in the contract of November 2, 1937, price schedules were not put into effect until the Sherwin-Williams Company and eleven other of the specified companies listed in the contract had agree to accept such licenses. On or about May 7, 1938, the required number of manufacturing companies having signed such agreements, the price schedules were made effective.

20. The license agreements between New Wrinkle and defendant K & S and between New Wrinkle

and the other licensed manufacturers of wrinkle finish provide, among other things, that:

a. Each licensee is licensed under New Wrinkle patents to make, use and sell wrinkle finishes;

b. Each licensee, in its sales of wrinkle finishes, is required to sell such finishes at not less than the minimum prices and discounts and on selling terms no more favorable than those established and to be established by New Wrinkle, except when selling to other licensees;

c. Each licensee agrees to pay a royalty of five cents per gallon on wrinkle finishes which it sells or uses;

d. Prices, terms and conditions of sale may be changed by New Wrinkle on 30 days' notice to each licensee and each licensee may cancel the agreement by giving written notice at any time during this 30-day period.

21. From time to time after May 7, 1938, knowing that concerted action among the defendants and co-conspirators was contemplated and required in order to carry out and maintain the aforesaid illegal combination and conspiracy and the aforesaid illegal contracts, other companies accepted licenses containing provisions similar to those described in paragraph 20 above. All of the license agreements are substantially identical. A copy of one of such agreements is attached to and made a part of this complaint as Exhibit C.

22. New Wrinkle, with the advice and consent of its licensees, from time to time has issued to all of such licensees schedules of minimum prices, terms and conditions of sale to be followed by each licensee in its sales of wrinkle finishes. Each licensee thereafter adhered to the minimum prices, terms and conditions of sale set forth in those schedules. A copy of the schedule in effect at the

present time is attached to and made a part of this complaint as Exhibit D.

V

EFFECT OF THE COMBINATION AND CONSPIRACY AND THE CONTRACTS

23. The combination and conspiracy and the contracts, and the acts done in effectuation thereof, hereinabove described, have had the effect, as intended by the defendants and co-conspirators, of fixing and maintaining identical and unreasonably high and arbitrary minimum prices, discounts and selling conditions and terms for substantially all wrinkle finishes manufactured and sold in the United States, and of eliminating competition between the defendants and co-conspirators in the sale of such finishes.

RELIEF

WHEREFORE, plaintiff demands:

(1) That the aforesaid combination and conspiracy and contracts be adjudged and decreed to be unlawful and in violation of Section 1 of the Sherman Act.

(2) That the aforesaid contracts and license agreements between the defendants and between the defendants, or either of them, and one or more of the co-conspirators, be declared to be illegal and be ordered terminated and cancelled.

(3) That the defendants and their officers, directors, agents, representatives, successors, assigns, and all persons and corporations acting on behalf of them or either of them be perpetually enjoined from combining, conspiring or agreeing to restrain trade and commerce in wrinkle finishes among the several states of the United States and with foreign nations, and that they be perpetually enjoined from engaging in or participating in practices contracts, relationships or understand-

ings, or claiming any rights thereunder, having the purpose or effect of continuing, reviving or renewing any of the aforesaid violations of the Sherman Act.

(4) That the Court adjudge and decree that the defendants have used their patent rights unlawfully in instituting, effectuating, and maintaining the aforesaid combination and conspiracy and the aforesaid unlawful contracts, and enter such orders relating to any and all of their patent rights as the Court may deem appropriate and necessary to dissipate the effects of the unlawful combination and conspiracy, contracts and activities herein alleged, and to establish free and unfettered competition in the trade and commerce herein described.

(5) That the plaintiff have such further, general and different relief as the nature of the case may require and the Court may deem proper in the premises.

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